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No. 84-716

In the Supreme Court of the United States

OCTOBER TERM, 1984

ARKANSAS LOUISIANA GAS COMPANY,
A DIVISION OF ARKLA, INC., PETITIONER

v.

FEDERAL ENERGY REGULATORY COMMISSION, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE FEDERAL ENERGY REGULATORY COMMISSION IN OPPOSITION

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QUESTION PRESENTED

Pursuant to regulations adopted by the Federal Energy Regulatory Commission, a natural gas pipeline company is permitted over a three-year period, .without having to resubmit its rates for a full review under Section 4 of the Natural Gas Act, 15 U.S.C. 717c, to change its previously established just and reasonable rates so as to recover on a current basis changing costs of the natural gas it purchases for resale. In return, the pipeline agrees to refile its rates with the Federal Energy Regulatory Commission for full review at least once every three years and, during that review, to collect those rates subject to refund.

The question presented is whether the Commission, on reviewing petitioner's triennial rate filing, complied with the requirements of the Natural Gas Act when it calculated petitioner's maximum refund liability with reference to the rate established as just and reasonable three years earlier in the previous full review procedure, rather than with reference to the rate as adjusted in the interim to recover increases in purchased gas costs.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 3a-6a) is unreported. The opinions and orders of the Federal Energy Regulatory Commission (Pet. App. 8a-17a, 18a-19a) are reported at 22 F.E.R.C. ¶ 61,125 and 23 F.E.R.C. ¶ 61,030. The opinion of the administrative law judge (reproduced in part at Pet. App. 20a-25a) is reported at 19 F.E.R.C. ¶ 63,008.

JURISDICTION

The judgment of the court of appeals (Pet. App. 1a-2a) was entered on June 14, 1984. A petition for rehearing was denied on August 8, 1984 (Pet. App. 7a). The petition for a writ of certiorari was filed on November 5, 1984. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1) and 15 U.S.C. 717r(b).

STATUTE AND REGULATION INVOLVED

Section 4(e) of the Natural Gas Act, 15 U.S.C. 717c(e), is reproduced at Pet. App. 27a-28a. The Commission's purchased gas adjustment regulation, 18 C.F.R. 154.38(d)(4), is reproduced at Pet. App. 30a-41a.

STATEMENT

1. Under the Natural Gas Act, 15 U.S.C. 717 *et seq.*, the Federal Energy Regulatory Commission has jurisdiction over wholesale rates charged by interstate pipelines for the sale and transportation of natural gas in interstate commerce. Section 4(d) of the Act, 15 U.S.C. 717c(d), provides that before a pipeline may increase its rates, it must file with the Commission a new rate schedule showing the changes to be made. Section 4(e) of the Act provides that the Commission may order a hearing on the lawfulness of the new rate filing and may suspend the effectiveness of the new rate for up to five months, after which the pipeline may collect the new rate, subject to refund. In *FPC* v. *Sunray DX Oil Co.*, 391 U.S. 9, 24 (1968), this Court held that if the Commission grants refunds under Section 4(e), they must be limited to the amount of the increase requested under Section 4(d).

One of the most volatile elements of a pipeline's rates is the cost of the gas it purchases for resale. Until 1972, a pipeline could obtain a rate increase based on changes in this single cost element only by submitting a full-scale general rate increase filing under Section 4 of the Act, 15 U.S.C. 717c. In 1972, the Commission promulgated a regulation authorizing pipelines to make adjustments to their filed and approved rates to reflect changes in their cost of purchased gas. Order No. 452, 47 F.P.C. 1049 (1972), amended, Order No. 452-A, 47 F.P.C. 1510 (1972), codified at 18 C.F.R. 154.38(d)(4). The tariff provisions authorized by this regulation are called "purchased gas adjustment" or "PGA" clauses. The provisions "permit pipeline companies to protect themselves against supplier rate increases without frequent general rate increase applications;" help to prevent

"prolonged delays in the final determination of proper rate levels [that] frustrate the administrative process;" and serve the interest of the ultimate consumer by requiring that companies "automatically reduce rates to reflect purchased gas decreases" and by providing for "periodic review and investigation into the companies' total cost of service." 47 F.P.C. at 1050-1051; Pet. App. 21a-22a.

The purchased gas adjustment regulation is not mandatory; the decision whether to recover purchased gas costs through Section 4 general rate filings or through the PGA mechanism is left to the company. 18 C.F.R. 154.38(d)(4)(ix). If a company elects the PGA alternative, it may adjust its filed "base tariff" rates every six months to reflect changes in its current cost of purchased gas, based on updated purchased gas data submitted to the Commission. 18 C.F.R. 154.38(d)(4)(iv)(*a*). In this way, a company may change its rates semiannually without the comprehensive rate increase application and full reexamination of cost-of-service data required in a Section 4 general rate case. PGA increases are authorized without consideration of any increases or decreases in other types of costs incurred by a company.

In return for the convenience of using the purchased gas adjustment mechanism, a pipeline must agree to file a restatement of its rates in order to establish a new base tariff rate at least once every three years. 18 C.F.R. 154.38(d)(4)(vi)(*a*). This triennial filing must be supported by a full cost of service study covering both purchased gas costs and other costs. Like any Section 4 general rate filing, the triennial filing is subject to Commission review and approval. If a pipeline charges the new rate for which it seeks approval during the period prior to Commission action, the Commission may order a refund to customers.

18 C.F.R. 154.38(d)(4)(vi)(*a*). However, the refund obligation is limited to the amount collected in excess of the old base tariff rate established three years earlier. 18 C.F.R. 154.38(d)(4)(vi)(*c*). See also Order No. 452-A, 47 F.P.C. at 1511.

2. Petitioner is an interstate natural gas pipeline company that has chosen to include the PGA clause in its tariff. In April 1980, petitioner filed a proposed general rate increase under Section 4 of the Act. The Commission initially suspended the effectiveness of petitioner's 1980 rate filing; on November 1, 1980, the proposed rate went into effect subject to refund pending administrative proceedings. Petitioner's rates had last been established in connection with a full Section 4 filing in November 1977;[1] since that time, petitioner had increased its rates semiannually through its PGA clause.

The administrative law judge (ALJ) concluded (Pet. App. 24a) that the rate change proposed by petitioner in 1980 was excessive. The ALJ rejected, inter alia, petitioner's contention that any refund liability must be calculated with reference to its 1977 base tariff rate as increased by the PGA adjustments it had made in the intervening period. The ALJ concluded instead that the 1977 base tariff rate itself established the floor to be used for calculation of petitioner's refund liability. *Id.* at 20a-24a. The net result was an order requiring a relatively modest refund consisting of the proposed rate increase from the time it took effect on November 1, 1980, and, for the same period, a small part of the portion of the rate representing PGA increases. Pet. 6-7.

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[1]The Commission reviewed petitioner's 1977 filing in *Opinion No. 71*, 10 F.E.R.C. ¶ 61,027 (1980), rev'd in part and remanded, 654 F.2d 435 (5th Cir. 1981), on remand, *Opinion No. 71-A*, 19 F.E.R.C. ¶ 61,012 (1982), aff'd, 701 F.2d 171 (5th Cir. 1983).

The Commission affirmed in a per curiam opinion (Pet. App. 10a-17a), in which it rejected all of petitioner's exceptions to the ALJ's decision. The Commission subsequently denied petitioner's request for rehearing (*id.* at 18a-19a). In doing so, it specifically rejected petitioner's claim that the Commission had imposed unauthorized retroactive refund liability. The Commission noted that its intervening decision in *Florida Gas Co.*, 19 F.E.R.C. ¶ 61,293 (1982), supported the ALJ's conclusion on this point.

3. The court of appeals affirmed in an unpublished per curiam opinion (Pet. App. 3a-6a). The court rejected, inter alia, petitioner's claim that the Commission had imposed improper retroactive refund liability in this case. The court stated (*id.* at 3a-4a):

> We can find no fault with FERC's interpretation and application of the PGA clause to the facts at hand. The interim streamlined filings by petitioner do not establish a new base rate below which refunds may not be ordered, for those rates are not subject to full FERC review until the triennial filing. Accordingly, it was proper for FERC to go back to the earlier 1977 base rate in fixing the floor on petitioner's refund liabilities.

ARGUMENT

The unpublished decision of the court of appeals is correct and does not conflict with any decision of this Court or any other court of appeals. Further review is therefore unwarranted.

1. Petitioner contends that each of its six-month purchased gas adjustments raised the floor used to calculate its refund liability in connection with its subsequent triennial filing to establish a new base tariff rate. Under petitioner's view, only a small part of its post-1977 rate increases (*i.e.*, that increase sought in the 1980 filing itself) was subject to refund during the period when the 1980 proposed rates were in effect.

The Commission's regulations clearly do not support the limitation on refund liability for which petitioner contends. The PGA regulation states that the refund obligation in connection with the triennial filing "shall be limited to the amount collected in excess of the old Base Tariff Rate." 18 C.F.R. 154.38(d)(4)(vi)(*c*). In clarifying the regulation soon after it was promulgated, the Commission stated explicitly that the refund floor would not be adjusted to take account of interim PGA adjustments (47 F.P.C. at 1511):

> It should be noted that the refund floor is the old Base Tariff Rate and is not the last effective rate (*i.e.*, the last Rate After Current Adjustment). This refund floor minimizes the possibility that companies will be able to retain revenues in excess of their cost of service and permits the extent of potential liability for refunds to be known.

See also 47 F.P.C. at 1051 (noting that the PGA regulation provides for "periodic review and investigation into the companies' total cost of service").[2]

Petitioner contends, however, that the Commission has exceeded its statutory authority in providing for calculation of refund liability with reference to the old base tariff rate, rather than the old rate as modified by intervening PGA adjustments. Petitioner cites in particular Section 4(e) of the Act, which authorizes refund of the portion of "increased rates" the Commission finds to be unjustified, and this Court's statement in *FPC* v. *Sunray DX Oil Co.*, 391 U.S.

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[2]Petitioner's suggestion (Pet. 16-17) that the language of the Commission's regulation does not support the result in this case is without merit. The regulation uses the term "Base Tariff Rate" with reference to the rate established and approved in connection with a triennial filing, not the rate as increased by subsequent PGA adjustments. Even if the regulation were ambiguous on this point, the Commission's subsequent clarification would remove any uncertainty on the part of pipelines that elect the PGA alternative.

at 24, that "an initial price which is authorized in a final, unconditional permanent certificate is a lower limit below which a refund cannot be ordered under § 4(e)." Petitioner claims that the statute and the Court's decision stand for the principle that the Commission may not order a retroactive rate reduction below the "previously established rate" (Pet. 13) and that the six-month PGA increases constitute part of that previously established rate.

Nothing in Section 4(e) of the Act suggests that PGA adjustments automatically become part of the "initial price which is authorized in a final, unconditional permanent certificate" (391 U.S. at 24). Indeed, petitioner's contention reflects a fundamental misunderstanding of the PGA procedure. The Administrative Law Judge correctly noted that PGA clauses are an administrative creation; they constitute "a divergence from the usual ratemaking procedures * * * and are allowed only as a stop gap measure to alleviate administrative backlog and to protect pipelines against supplier rate increases without frequent general rate increase applications" (Pet. App. 23a). The PGA mechanism in no way substitutes for the "periodic review and investigation into the companies' total cost of service" (*id.* at 22a). The Eleventh Circuit recently described the relationship between PGA adjustments and the triennial filings to establish new base tariff rates:

> The Commission has a statutory duty to ensure that pipeline rates are "just and reasonable." 15 U.S.C.A. §§ 717c-717d. Although it has permitted pipelines through PGAs to pass on to consumers increases in the cost of purchased gas without regulatory review, it requires the pipelines to restate their base tariff and submit a full cost study every 36 months. * * * Through this periodic review, the Commission seeks to protect consumers from excessive rates.

South Georgia Natural Gas Co. v. *FERC*, 699 F.2d 1088, 1091 (11th Cir. 1983). See also *Florida Gas Transmission Co.* v. *FERC*, 741 F.2d 1307, 1309 (11th Cir. 1984); *El Paso Natural Gas Co.* v. *FERC*, 677 F.2d 22, 23 (5th Cir. 1982); *Panhandle Eastern Pipe Line Co.* v. *FERC*, 613 F.2d 1120, 1143 (D.C. Cir. 1979) (Wright, C.J., concurring in part), cert. denied, 449 U.S. 889 (1980).

By choosing to make PGA adjustments every six months, a pipeline knowingly avoids the full-dress review normally required to determine whether such increases would result in a just and reasonable rate. The three-year review that is required when a pipeline elects the PGA alternative ensures that the relation between the pipeline's rates and its total costs of service will not escape Commission scrutiny indefinitely as a result of the pipeline's use of the PGA mechanism. In these circumstances, it is entirely reasonable for the Commission to provide that it is the base tariff rate — *i.e.*, the last fully-reviewed rate based on the pipeline's total cost of service — that serves as the floor for calculation of refund liability; it is this rate "below which a refund cannot be ordered under § 4(e)" (*FPC* v. *Sunray DX Oil Co.*, 391 U.S. at 24) for the period when the proposed rate is in effect, but still under review. The Commission's reasonable interpretation of the statute it administers is entitled to deference. See *Chevron U.S.A. Inc.* v. *Natural Resources Defense Council, Inc.*, No. 82-1005 (June 25, 1984), slip op. 6.

2. Petitioner seeks to escape application of these principles by contending that, since it sought no increase in its purchased gas costs in connection with the Section 4 proceeding it instituted in 1980 (see Pet. 5-7), its PGA increases during the period 1977 through November 1, 1980 must be regarded as uncontested and as part of the established rate used in determining the refund floor. But that contention assumes that when the Commission examines a pipeline's total costs in connection with a triennial review it may not

take account of the effect of PGA increases since the last full review of costs. The courts of appeals have uniformly rejected such contentions.

The Eleventh Circuit, in reviewing the scope of a new base tariff rate filing made under the PGA regulations, recently stated that "all costs including the cost of purchased gas are included in the section 4 review and approval of the Base Tariff Rate." *Florida Gas Transmission Co.* v. *FERC,* 741 F.2d at 1311.[3] See also *Laclede Gas Co.* v. *FERC,* 670 F.2d 38, 41 (5th Cir. 1982) (the Section 4 rate filing "opened to Commission scrutiny the propriety of the [unchanged] PGA clause contained within its rate schedule"); *Cities of Batavia* v. *FERC,* 672 F.2d 64, 77 (D.C. Cir. 1982) (the Commission was not precluded "from reviewing a revised rate completely to assure that all its parts — old and new — operate in tandem to insure a 'just and reasonable' result and from ordering refunds if the previously approved [component] * * * operates with new provisions to produce an over-recovery").[4] These decisions

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[3] *Florida Gas Transmission Co.* v. *FERC* affirmed the decision the Commission cited as authority for rejecting petitioner's contention concerning retroactive refund liability (see Pet. App. 19a). The issue in *Florida Gas Transmission Co.* was whether a company that buys, resells, and transports gas, and that uses a PGA clause in connection with its resale rates, exposes its transportation rates (as well as its resale rates) to Commission scrutiny when it makes its required triennial base tariff rate review filing. The Eleventh Circuit affirmed the Commission's interpretation of the PGA regulation as providing that the company's transportation rates would be exposed to Commission scrutiny in such circumstances, even when those rates had remained unchanged. The court emphatically rejected the contention petitioner makes here —that only rate components a pipeline seeks to change at the triennial filing are subject to a refund obligation under the Natural Gas Act. 741 F.2d at 1311.

[4] *Cities of Batavia* involved the rate review provisions of Section 205 of the Federal Power Act, 16 U.S.C. 824d. However, that section is virtually identical to Section 4 of the Natural Gas Act; and this Court has recognized that precedent under one section is applicable to the other. *Arkansas Louisiana Gas Co.* v. *Hall,* 453 U.S. 571, 577 n.7 (1981).

are entirely consistent with the settled notion that "a natural gas company initiating an increase in rates under § 4(d) assumes the hazards involved in that procedure" (*FPC* v. *Tennessee Gas Transmission Co.*, 371 U.S. 145, 152 (1962)). The decisions indicate that PGA adjustments should not be regarded as settled components of an established, previously approved rate.

3. Petitioner's contention (Pet. 11-12) that the result below conflicts with *Distrigas of Massachusetts Corp.* v. *FERC (DOMAC)*, 737 F.2d 1208 (1st Cir. 1984), is without merit. The court in *DOMAC* merely reiterated the basic principles applicable to refund liability, as stated in Section 4 of the Act and in *FPC* v. *Sunray DX Oil Co., supra.* 737 F.2d at 1224. As we explained above, the result in this case is entirely consistent with those principles. *DOMAC* did not involve either a PGA clause or base tariff rates. Thus, the decision in that case clearly does not conflict with the result below.[5]

4. Petitioner implies (Pet. 5-7, 10-11, 15) that it has been unfairly required to disgorge amounts it collected long ago, during a time when it had no reason to believe those

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[5]Indeed, petitioner admits as much when it characterizes the issue in this case as "novel" (Pet. 9, 17).

If anything, *DOMAC* supports the result in this case. The court in *DOMAC* reviewed the Commission's interpretation of a rate settlement agreement as providing a particular refund floor. The court recognized that, in the absence of any agreement, DOMAC's refund liability would be limited to the amount of the requested rate increase. It nevertheless held that the Commission could enforce the settlement agreement, even if the result were that DOMAC would pay a larger refund amount than it otherwise would have been required to pay. 737 F.2d at 1224-1225. The PGA regulations can be viewed as creating a similar agreement. In exchange for the ability to use the PGA alternative, pipelines agree to use the base tariff rate established in the previous full review proceeding as the refund floor when their rates are reviewed. The Commission is entitled to enforce that agreement, as it did in this case.

amounts would be subject to refund. In fact, the Commission has not imposed any such liability. The order in this case does not require petitioner to refund any part of the rates it collected from 1977 to November 1, 1980 (the date when the new proposed rate went into effect following the 1980 triennial rate filing), including the amounts representing purchased gas adjustments. Even for the period after November 1, 1980, petitioner has been required to refund only a small part — 12.64 cents per Mcf — of its post-1977 PGA increases (which added up to 90.62 cents per Mcf), in addition to the 1980 proposed rate increase of 9.52 cents per Mcf. See Pet. 5-7. In any event, as we explained above (page 6 & note 2), Commission regulations put petitioner on notice that the floor for refund obligations applicable to rates charged after November 1, 1980, would be measured with reference to its 1977 base tariff rate. In these circumstances, petitioner can hardly claim that the refund order is unfair.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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